

The Artist as Entrepreneur

Is This a Hobby or a Business?

Lesson description

Many artists must maintain either full- or part-time employment in addition to their art activity to earn income. In this case, artists may find it difficult to claim expenses related to their art as business expenses because the IRS may consider the art activity to merely be a hobby. The artist, then, must be aware of the IRS criteria for establishing their activity as a business. In this lesson, students will learn the IRS criteria and list ways they might be able to demonstrate that their art activity (present or future) is actually a business venture.

Concept

Total revenue
Total cost
Profit/Loss
IRS criteria for operating a business in the arts

Lesson objectives

Students will:

Define total revenue and total cost
Define profit and loss
List ways that their art activity can be viewed as a business

Materials

Visual 1, *Is This a Hobby or a Business?*
Visual 2, *Be a Business*

Procedure

1. Ask students if they would describe their future plans as an artist as an entertaining pastime or as their life's work. Explain that artists may describe their art as their life's work – their occupation. However, if they want to convince the IRS that their art is their business, they must do more than simply state it as such.
2. Explain that for tax purposes activities earning profits in three of five years are normally presumed to be businesses rather than hobbies. Artists who meet this requirement are allowed to deduct their business expenses when they file their Schedule C, *Profit or Loss from Business*, with the IRS.
3. Explain that profit and loss have very specific meanings. Define total revenue as all of the money received from the sale of a product. Define total cost as all of the expenses related to the production of a product. Define profit as the money remaining after total costs have been subtracted from total revenue. Explain that if a

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company's total revenue is greater than its total cost, the company has earned a profit. If, however, total cost is greater than total revenue, the company has suffered a loss.

4. Remind students that the IRS considers an activity to be a business if it earns a profit for three of five years. Explain that many artists may have operated at a loss for five years, and they are concerned that the IRS auditor may declare their work as an artist to be a hobby rather than a business.
5. Display Visual 1, *Is This a Hobby or a Business?* Explain that according to Jo Hanson, author of *Artist's Taxes, The Hands on Guide – An Alternative to Hobby Taxes*, it is the artist's commitment to his art as a business that matters.
6. Explain that to help artists make a convincing case with the auditor, Hanson and other experts such as Floyd Conner, co-author of *The Artist's Friendly Legal Guide*, point to the nine factors the IRS considers in determining whether an artist is a hobbyist or a professional. The idea is to address each factor in the way you approach your work.
7. Display Visual 2, *Be a Business*. Explain each point as follows:
 - **Do you carry on your activity in a business-like manner?** First and foremost, be sure you have complete records of your business transactions. Open a bank account in the name of the business. And, be sure you look like a business. Create a logo for your business and use it on letterhead, business cards, and brochures.
 - **Does the time and effort you spend on the activity indicate that you intend to make it profitable?** Record the amount of time you spend working on your art. The more time you spend on your art business, the more likely you will be viewed as having a serious dedication to promoting your business.
 - **Do you depend on income from your art for your livelihood?** An apparent need for income will support your case. Keep records of the ways you sought income.
 - **Are the losses you sustain in your art business due to circumstances beyond your control?** Your losses may be due to heavy investment in start-up costs.
 - **Can you change your methods to improve your profitability?** You should review your methods of production and marketing regularly. Look for ways to acquire your materials more inexpensively, or find alternative materials that suit your purposes. Seek alternative ways to market your art, or seek new markets. Consider creating additional goods that would be purchased along with your art. Goods that are purchased together are referred to as complements. For example, if your art includes production of ceramic plates, you might consider designing stands for the plates.

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- **Is your art business ever profitable?** If you are able to show that you earned a profit in some years, your claim as a business is more credible. Is there one particular aspect of your business that is profitable? Examine each type of product you make to determine if one or more of your lines is profitable.
- **Do you, or your advisors, have the knowledge needed to build and sustain a successful art business?** If your legal and accounting skills are not adequate, get some help. Entrepreneurs are devoted to providing their product. It is rare to find entrepreneurs who are skilled in all aspects of business development. It is important to hire the services of experts, particularly in taxes and contracts. As your knowledge in these areas improves, you will need expert services less.

In some localities, you may be able to find such services free of charge. Check to see if your community has a Volunteer Lawyers and Accountants for the Arts (VLAA) organization, a Service Corp of Retired Executives (SCORE) office, or a Small Business Development Center (SBDC). The VLAA is a non-profit group in support of the arts. SCORE and SBDC are supported through the U.S. Small Business Administration.

- **Have you been successful in making a profit in similar activities in the past?** Cite teaching, jurying, curating, and writing in addition to examples of your previous art businesses.
 - **Can you expect to make a future profit from the appreciation of the assets used in your art business?** If your sales and selling prices have increased, then you can demonstrate a reasonable expectation of future profits. Because an artist's reputation typically grows over time, your unsold work should also appreciate in value.
8. If any of the students in class are already operating as a business, ask them to explain in what ways they are addressing the items on the *Be a Business* list. Place students into groups. Instruct each group to list at least five things that they could accomplish right now to give their art the appearance of a business.
 9. OPTIONAL: Instruct students to design a logo for their business and create business cards, letterhead, and/or brochures.

Closure

Provide an overview of the lesson by asking the following questions:

What is total revenue? (*Total revenue is all of the money received from the sale of a product.*)

What is total cost? (*Total cost is all of the expenses related to the production of a product.*)

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What is profit? (*Profit is the money remaining after total cost has been subtracted from total revenue.*)

What is loss? (*Loss is a shortfall, where total cost exceeds total revenue.*)

What can an artist do to define his activities as a business rather than just a hobby?
(*Answers will vary, but students should reflect on the Be a Business list.*)

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Visual 1

Is This a Hobby or a Business?

“If you can establish that you produce art as your primary commitment and have the on going intention of making a profit from it, then you are entitled to deduct the expenses of your art business, even if you fail to make a profit year after year. The legitimate attempt is what has to be proved.”

Jo Hanson

Artist's Taxes, The Hands on Guide – An Alternative to Hobby Taxes

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Visual 2

Be a Business

Do you carry on your activity in a business-like manner?

Does the time and effort you spend on the activity indicate that you intend to make it profitable?

Do you depend on income from your art for your livelihood?

Are the losses you sustain in your art business due to circumstances beyond your control?

Can you change your methods to improve your profitability?

Is your art business ever profitable?

Do you, or your advisors, have the knowledge needed to build and sustain a successful art business?

Have you been successful in making a profit in similar activities in the past?

Can you expect to make a future profit from the appreciation of the assets used in your art business?